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ABSTRACT

This paper analyzes the negative effects on private colleges of state subsidies provided to state-run colleges, noting the increasing proportion of students attending public colleges and the closing of more than 300 private colleges between 1969-70 and 1992-93. It urges legislators to eliminate direct subsidies to universities, to require universities to charge tuition sufficient to cover costs, and to give financial aid directly to students. The first section considers effects of government subsidies on college tuition and the shift in enrollment from private to public colleges. Next, the British experience with primary and secondary education is reviewed to illustrate the reduction of a dominant private sector to a minority role. Third, the situation in three states is reviewed: New York, a large state with a high ratio of private-to-public enrollment; California, a large state with a low ratio of private-to-public enrollment; and Vermont, a small state with a low reliance of public colleges and universities on state government funding. The following section focuses on the importance of private higher education, emphasizing the special characteristics of private colleges, their contribution to the social order, and their economic efficiency. The final section examines various solutions to this problem. (Contains 70 endnotes.) (DB)

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Public Subsidies and Private Colleges

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Executive Summary

State governments spent more than $44 billion on higher education in 1995-96. Legislators should consider the effect that direct provision of higher education has on private colleges and universities.

Private colleges are essential to diverse and independent education and to the maintenance of a civil society independent of the state.

Heavy subsidies to state-run colleges are making life difficult for the independent sector of higher education. In-state tuition covers only about 28 percent of the costs of providing an education in a public college.

At the beginning of this century, more than four of every five students were enrolled in private colleges. Now almost four of every five students are enrolled in public universities. Economic analysis suggests--not surprisingly--that below-cost tuition at public colleges draws students away from the private sector. More than 300 private colleges closed their doors between 1969-70 and 1992-93.

Legislators should stop using below-cost tuition to lure students from private to public colleges. They should eliminate direct subsidies to universities, require the universities to charge tuition sufficient to cover costs, and give financial aid directly to students, to be spent at either public or private colleges. Otherwise, we may eliminate a vital part of civil society.

Gary Wolfram is George Munson Professor of Political Economy at Hillsdale College in Michigan.

State governments are heavily committed to their college and university systems. In fiscal year 1995-96, they spent more than $44 billion for ongoing higher education operations. More than 1,500 public colleges and universities in the United States enroll more than 11 million students. And more than 2,000 private colleges and universities exist alongside the system of state-government-controlled higher education. Since those two systems are, in many ways, substitutes for one another, state legislators should consider the effect that direct provision of higher education by the state has on private colleges and universities.

The combination of state-run and private, independent higher education is an important characteristic of the American system. As George Roche, president of Hillsdale College, has pointed out, "There is, simply, no other system like ours. By contrast, Great Britain has one private university; Germany has one; Australia has none. France and Japan together have a few hundred, but they are highly subsidized and/or regulated by the state. With all its faults, our system is the freest and most independent."[1]

It is that freedom and independence that must be preserved. There are many practical reasons why we would want to maintain a strong private sector in higher education, such as the economic inefficiencies of government-provided services and the ability to offer certain programs only in a private setting. However, the most important is that an education provided by the government is likely to reflect the beliefs and priorities of those in charge of the political system. One need not agree with John Stuart Mill that "a general State education establishes a despotism over the mind"[2] to recognize that the only way to ensure a truly independent educational system is through a strong private sector.

It is also only through a system of private colleges that a diverse and plural education is possible. As an example, religion is controversial, and there is great difficulty in treating the role of religion in the classical higher education curriculum within the confines of a state-run institution.[3] True diversity of thought can lead to a backlash from a legislature hearing from its constituents about their tax dollars being spent to promote differing ideas. And private colleges provide the moral order necessary for the maintenance of a free and civil society.

Early on, private colleges understood the interaction between primarily private education and state-owned and

state-operated colleges. In 1872, when Congress was debating whether to increase the federal endowment of land-grant colleges, the presidents of Harvard and Princeton spoke out strongly against federal endowments.[4] Yet, as William Zumeta has noted after examining a survey of state higher-education-agency executives, today the "effects on independent institutions are rarely taken into account in public tuition policies."[5]

By providing the major share of revenue for state institutions of higher learning, legislators have created a situation in which state colleges and universities may charge tuition far below the cost of providing educational services and underprice their private counterparts. That disadvantages private colleges and universities and makes it difficult for them to retain their share of student enrollment. Higher education ought to be provided through the private sector for many reasons independent of the role of state government in funding those services. As state governments examine their role in higher education, they should consider providing subsidies directly to students much as the federal government has done through the G.I. Bill, Pell grants, and guaranteed student loans.

The Effect of Public Higher Education on Private Higher Education

There is good evidence that state government subsidies allow public colleges and universities to charge tuition that is substantially less than the cost of education and to underprice the private sector and thus to lure students from private to state-run colleges.

Government Subsidies and College Tuition

The primary source of revenue for public colleges and universities is state government, while the primary source of revenue for the private sector is tuition (Table 1).

State governments, over the past 20 years, have been the source of about two of every five dollars of operating revenue for public institutions of higher education. State government funds for current-fund revenue increased in current dollars from slightly less than $18 billion in 1979-80 to $39.7 billion in 1992-93.[6] Although since 1985-86 state governments have gradually declined as a source of current-fund revenue, from 45.0 percent to 36.8 percent,

Table 1
Sources of Revenue as a Percentage of Current-Fund Revenue for Public and Private Institutions

Year	State Gov't--Public	State Gov't--Private	Tuition and Fees--Public	Tuition and Fees--Private
1980	46.3	2.1	12.5	35.9
1981	45.6	1.9	12.9	36.6
1982	45.3	1.8	13.5	37.6
1983	44.8	1.9	14.5	38.6
1984	44.3	1.8	14.9	38.8
1985	45.1	1.9	14.5	38.7
1986	45.0	1.9	14.5	38.6
1987	43.7	2.2	14.7	39.6
1988	43.4	2.5	15.0	39.1
1989	42.5	2.6	15.2	39.4
1990	41.7	2.6	15.5	39.6
1991	40.3	2.3	16.1	40.4
1992	38.3	2.5	17.1	40.7
1993	36.8	2.3	18.0	41.2

Source: U.S. Department of Education, National Center for Education Statistics, Digest of Education Statistics, various years.

they still provide the lion's share of funding for operating expenses of the public college and university system.

State governments, on the other hand, are a minor source of revenue for private colleges and universities, ranging from 1.8 percent of current-fund revenue to 2.6 percent over the period 1979-80 to 1992-93. In current dollar amounts, state governments provided slightly more than $400 million to private colleges and universities in 1979-80; that amount rose to slightly less than $1.5 billion in 1992-93.

Tuition and fees for public institutions are significantly less important as a source of revenue than are state government subsidies. Although they gradually rose in percentage terms, after making up 12.5 percent of current-fund revenue in 1979-80, they still made up only 18.0 percent of such funds in 1992-93. Tuition and fees rose in current dollar terms as well, from $4.9 billion in 1979-80 to $19.5 billion in 1992-93, yet they remained only about half as important as state governments as a source of current-fund revenue for public institutions.

Tuition and fees are the major source of revenue for private colleges and universities. Tuition and fees rose gradually from 35.9 percent of current-fund revenue in 1979-80 to 41.2 percent in 1992-93. In current dollars, they rose from $7 billion to $25.9 billion. Thus, for private colleges and universities, tuition and fees are nearly 20 times as important as a source of current-fund revenue as is state government funding.

State government subsidies to the public college and university system allow the institutions to charge lower tuition than the private schools. Some evidence of that is found in the data just discussed on their relative reliance on tuition and fees. More direct evidence is a comparison of average tuition and fees of the two systems (Table 2). The data show clearly that public colleges and universities charge substantially lower tuition than do private colleges and universities.

Tuition and fees at public institutions of higher education have historically been a fraction of those charged by private ones. Using current dollars, in 1964-65 public institutions were charging an average of $243 for in-state undergraduate tuition and fees, while the private sector's tuition and fees averaged $1,088. Although tuition and fees rose at public colleges to $2,057 in 1994-95, private tuition and fees rose to $11,128 (Figure 1). Over the last three decades, tuition and fees at private colleges and universities have been more than five times as high as those at public ones. In current dollars, the gap has widened from $845 to more than $9,000.[7]

As further evidence that state funding allows states to charge below-cost tuition and underprice private colleges, the General Accounting Office found that the average education-related expenditure per student in public four-year colleges and universities in the 1993-94 school year was $8,892 (Figure 2). The average in-state tuition was 28 percent of that, $2,525.

Although the ratio of expenditure to tuition and fees varied by state, only New Hampshire and Vermont charged an average in-state tuition that was at least half of the cost of providing the educational service.[8]

The GAO also found that tuition levels at public four-year colleges and universities across states were statistically related to the percentage of current revenues provided by state government. Using data for the 1993-94 school year, the GAO noted that in the 10 states in which state

Table 2
Average Undergraduate In-State Tuition and Fees (current dollars)

Year	Public (in-state)	Private
1965	243	1,088
1966	257	1,154
1967	275	1,233
1968	283	1,297
1969	295	1,383
1970	323	1,533
1971	351	1,684
1972	376	1,820
1973	407	1,898
1974	438	1,989
1975	432	2,117
1976	433	2,272
1977	479	2,467
1978	512	2,624
1979	543	2,867
1980	583	3,130
1981	635	3,498
1982	714	3,953
1983	798	4,439
1984	891	4,851
1985	971	5,315
1986	1,045	5,789
1987	1,106	6,316
1988	1,218	6,988
1989	1,285	7,461
1990	1,356	8,147
1991	1,452	8,722
1992	1,624	9,434
1993	1,782	9,942
1994	1,942	10,572
1995	2,057	11,128

Source: U.S. Department of Education, National Center for Education Statistics, Digest of Education Statistics, various years. Data are for all institutions.

appropriations provided 50 percent or more of the public schools' revenues, the average tuition was about $2,000, or 21 percent, below the national average for that year. In the eight states where state appropriations provided 35 percent

Figure 1
Tuition and Fees

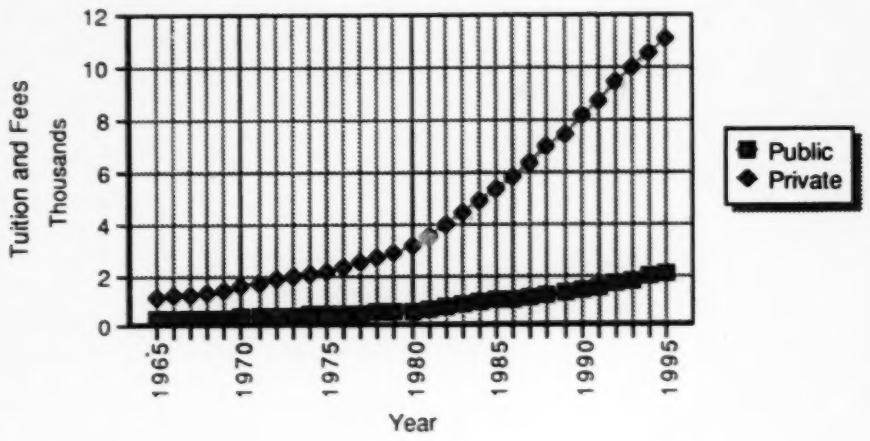
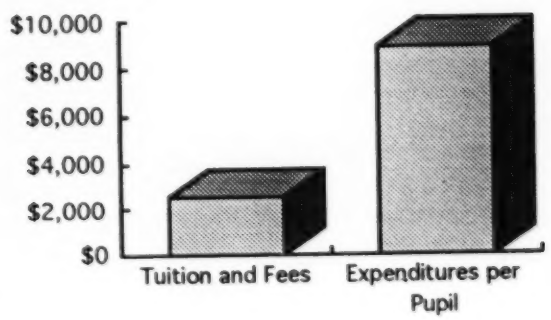


Figure 2
Tuition and Expenditures per Pupil, Public Institutions, 1993-94



or less of public institutions' revenue, the average tuition was about $3,500, or 38 percent, above the national average for that year.[9] In a multiple regression analysis, the GAO found that state appropriations per full-time equivalent student were highly correlated with average tuition levels at public institutions and explained about 22 percent of the variation in tuition across states.[10]

A simple regression of average tuition at all public colleges and universities on the percentage of current-fund revenue coming from state sources yields results similar to those of the GAO study. Using 1992-93 state data, the coefficient on state funding is highly significant, and the simple regression explains 44 percent of the variation in tuition levels.

It is abundantly clear that state support of public colleges and universities is translated into lower tuition rates relative to private colleges and universities. Basic economic theory, as well as common sense, tells us that consumers will consider price differences in choosing between two goods that are substitutes for each other. Everything else being the same, we will choose one provider of a service over another if the first provider's price is lower. In the case of public and private higher education, of course, not everything else is the same. However, a substantial price differential, such as has been the case over the last three decades, should have a significant effect on students' choices of public or private colleges.

Several studies indicate that is the case. A survey of the literature by Michael McPherson found that "reduced tuition rates at public institutions would raise public enrollment, but the rise will come in large part at the expense of private enrollment."[11] McPherson suggested that during the 1960s the rise in the tuition gap accounted for somewhat less than half of the shift in enrollment from private to public institutions that took place during that time. McPherson found that the effect differed by type of institution. A regression analysis using 1972 data found "a quite strong effect of public tuition levels on enrollments at less selective liberal arts colleges and a very weak effect on private research and doctoral-granting universities."[12]

Using a statistical technique that estimates the probability of a student's attending a college, Charles Manski and David Wise found that tuition levels have a negative effect on the probability that a student will choose a college or university, indicating that the differences in public and private tuition affect the level of enrollment in public and private institutions.[13] Larry Leslie and Paul Brinkman provide a survey of the literature on student price responses to higher education. They conclude that student price sensitivity is greatest in the least selective institutions and that low-income students are more price sensitive than higher income students.[14] That is consistent with McPherson's findings.

Using survey data to focus on the effect of tuition increases at elite private institutions, McPherson and Morton Shapiro found "the fact that the relative success of private institutions in attracting middle- and lower-income students seems to depend heavily on institutionally financed student aid may also be a cause for concern."[15] That finding, combined with their other finding that high-PSAT students who do not apply to elite private institutions disproportionately attend public colleges and universities, is consistent with the economic reasoning that lower tuition at public institutions affects enrollment at private ones. Indeed, they offer the following concern: "While the 'elite' and usually well-endowed private institutions have thus far provided enough financial aid to mute potential enrollment effects resulting from the growing divergence between their prices and the prices at public alternatives, other private institutions may not be able to do the same."[16]

Recently Philip Ganderton found, using survey data and a probability model, that students trade off private college quality for lower tuition in the public sector.[17] Charles Kroncke and Rand Ressler, using a regression model with state data for fiscal years 1986 and 1987, argue that changing relative prices of public to private higher education changes the enrollment ratio.[18] Those studies, among others, are consistent with the prediction of economic theory that tuition price advantages at public colleges and universities will increase student demand for those institutions relative to private colleges and universities.

The Shift in Enrollment

Enrollment data support the claim that public colleges and universities, subsidized directly by state governments, are capturing an expanding share of enrollment. At the beginning of this century, more than four of every five students were enrolled in private colleges and universities.[19] By the middle of the century, about one-half of college students were enrolled in private colleges and universities. From the 1960s on, the decline in private school enrollment accelerated (Table 3). By 1990 the composition had reversed itself from the beginning of the century, with almost four of five students enrolled in public universities.

During the three decades from 1965 to 1995, total fall enrollment in public institutions increased by 7.038 million students, whereas enrollment in private institutions in

Table 3
Total Fall Enrollment (thousands of students)

Year	Public	Private	Year	Public	Private
1959	2,181	1,459	1986	9,714	2,790
1965	3,970	1,951	1987	9,973	2,793
1970	6,428	2,153	1988	10,161	2,894
1975	8,835	2,325	1989	10,578	2,961
1980	9,457	2,640	1990	10,845	2,974
1981	9,647	2,725	1991	11,310	3,049
1982	9,696	2,730	1992	11,385	3,101
1983	9,683	2,782	1993	11,189	3,117
1984	9,477	2,765	1994 est.	11,008	3,074
1985	9,479	2,768	1995 proj.	11,108	3,101

Source: U.S. Department of Education, National Center for Education Statistics, Digest of Education Statistics, 1995, and Projections of Education Statistics to 2006.

creased by 1.123 million. The public sector thus absorbed more than 86 percent of the enrollment increase.

Much of the enrollment increase in the public system has been at the two-year-college level. From 1965 through 1994, enrollment in public two-year colleges increased from 1.041 million to 5.177 million. During that period, two-year colleges went from 26 percent of public college enrollment to 47 percent. Two-year colleges have been much less of a factor in the private system. Private two-year-college enrollment went from 132,000 in 1965 to 238,000 in 1994. Two-year colleges thus represented 6.7 percent of private college and university enrollment in 1965 and only 7.7 percent in 1994.

It is in the expanding two-year public college system that the tuition differential between the private and public sector is greatest. Tuition and fees in 1994-95 at two-year public colleges were only $1,194. That compares with $11,522 at the private four-year college or university, where 92 percent of private institution students are enrolled, and $6,865 for private two-year colleges.

A regression of the ratio of private institution enrollment to public institution enrollment by state on state average tuition and fees at public institutions, using state data for the 1992-93 school year, supports the conclusion

that lower tuition levels at state schools reduce private-sector market share. The simple regression of public tuition and fee levels explained about 44 percent of the variance in the private/public enrollment ratio. When the regression included the number of private and public colleges ranked nationally by U.S. News and World Report,[20] the regression explained 60 percent of the variance, while the effect of public tuition and fee levels remained statistically significant and stable.[21]

Another fee comparison, of tuition and fees charged for in-state residents and out-of-state residents at public colleges, indicates that in-state residents are being charged below-market rates. Examples are given in Table 4.

The range of tuition at state-run schools shows a clear pattern of state subsidy for resident students. There is

Table 4
In-State and Out-of-State Tuition, 1996-97 Academic Year (current dollars)

School	In-State	Out-of-State
Arizona State University	2,009	8,377
Arkansas State University	1,970	5,060
U.C. Berkeley	4,354	12,748
University of Colorado	3,309	15,022
University of Connecticut	4,794	13,244
University of Florida	1,830	7,100
University of Illinois	4,153	10,453
Indiana State University	3,072	7,604
University of Kentucky	2,674	7,354
University of Maryland	4,169	10,228
University of Massachusetts	5,465	12,195
Michigan State University	5,501	13,037
Rutgers University	5,105	9,277
SUNY-Buffalo	4,060	8,960
Clemson	3,170	8,478
Middle Tennessee State University	2,022	8,380
University of Texas-Austin	2,568	8,988
Virginia Tech	4,131	11,415
Washington State University	3,249	8,933

Source: Editors of U.S. News and World Report, America's Best Colleges: The 1997 Directory of Colleges and Universities.

little reason to believe that differences in demand between in-state and out-of-state students are sufficiently large that the pricing scheme represents some form of marginal cost pricing. The most plausible reason for the large and consistent price differential is that public colleges and universities are charging their resident students a taxpayer-subsidized tuition that cannot be politically justified for nonresidents.

We seem now to have reached a steady-state equilibrium, with the National Center for Education Statistics projecting the ratio of private to public enrollment rising slightly from .279 to .283 from 1995 to 2006. The massive shift to the public system may be behind us, but there is no indication that, without a substantial change in the method of funding public colleges and universities, the private sector will make any advances over the next decade.

Because private institutions of higher education are on average much smaller than public institutions, enrollment figures give a better picture of the growth of the public sector relative to the private sector than do data on the number of institutions. Just examining the number of institutions, one would find that the number of private colleges and universities increased from 1,571 in 1974-75 to 2,047 in 1994-95, while public colleges and universities during the same period went from 1,433 to 1,641.[22] But average enrollment is clearly much greater in public institutions; it rose from 6,165 in 1974-75 to 6,769 in 1994-95. Average enrollment in private institutions of higher education rose from 1,496 to 1,515 over the same period. In 1993 all but 8 of the 120 institutions of higher education with the largest enrollments were public.

When looking at the number of institutions, it is interesting to look at what has happened to traditional four-year private liberal arts colleges. The Carnegie Foundation classified 540 private liberal arts colleges in 1987.[23] Over the past 10 years that number has remained relatively stable, with the National Center for Education Statistics reporting 533 colleges with the Carnegie classification in 1995.[24] While the private sector has managed to hold on to its 20 percent share of students and to create some new schools, the traditional liberal arts college sector has remained stagnant. In fact, David Breneman argues that many of the liberal arts colleges have altered their curricula to provide more of a science and business degree to compete with the mass education of the state systems. Using his classification, the number of true liberal arts colleges has declined substantially.[25]

What may be more telling than the change in the total number of institutions as a result of pressure on private, independent colleges and universities from discounted tuition at state-run colleges and universities is the number of institutions that have closed their doors. From 1969-70 to 1992-93, of the 346 institutions of higher education that closed their doors, 312 were private. Thus, the private sector is a more dynamic, threatened environment, marked by a few small new entrants and a failure rate far exceeding that of the public institutions.

The British Experience with Primary and Secondary Education

The pattern of a dominant private sector being reduced to a minority role in providing education is a repetition of what happened to the primary and secondary schools in England in the 19th century. E. G. West has traced the effect of the Education Bill of 1870 on Great Britain's private school system.[26] In the debate in Great Britain about whether to establish state schools in what was, at the time, a school system composed almost entirely of private schools, Henry Brougham pointed out that parents forced to pay taxes to support a state school would not only have a substitute for a private school that relied on tuition; they would also have less disposable income to pay tuition. In May 1835, he remarked on the floor of the House of Commons:

> Let the tax gatherer, or the county-assessor, or the parish collector, but once go his rounds for a school rate, and I will answer for it, that the voluntary assistance of men in themselves benevolent, and indeed, munificent, instead of increasing, will soon vanish away; that the 1,144,000 now educated at unendowed schools will speedily fall down to almost nothing; and that the adoption of such a fatal and heedless course will sweep away those establishments which, at present, reflect so much honour on the community, which do so much good and are calculated, with judicious management, to do so much more.[27]

West cites evidence to suggest that the institution of public schools, called Board schools, caused a substantial shift of students from private schools to the new public schools. His logic to explain that phenomenon is also applicable to the situation of U.S. higher education today.

> Altogether then, the "competition" of the Board Schools with private schools was one which the

> latter could rarely hope to win. But if conditions were hostile to existing private schools they were even more discouraging for potential newcomers. Only the boldest of individuals were prepared to attempt to trade without a bounty in competition with those who traded with a considerable one (to use the words of Adam Smith).[28]

West's latter point leads us to consider not only the failure rate of private schools but the ability of private schools to capture new market share. The evidence presented above on enrollment indicates that private colleges and universities have little ability to enter the market for higher education to any large effect.

Public universities and private colleges are not perfect substitutes for each other. Private colleges tend to be smaller, have a stronger emphasis on undergraduate teaching, and offer a different atmosphere from a 40,000-student state university. The existence and tuition policies of public colleges, while putting stress on private colleges and altering their behavior, will probably not eliminate the private college. Some are doing very well. However, only those private colleges that can establish the uniqueness of the product they offer will survive.

State Examples

There is substantial variation among the states in the reliance of public colleges and universities on state funding. As a percentage of total current-fund revenue, in 1992-93 the range was from 15 percent in Vermont to almost 64 percent in Hawaii. The average ratio was 37 percent. Despite the variation, the reliance on state funding was in every state far above the national figure for private schools of 2.3 percent.

To get a feel for the situation in various states, this section provides a brief discussion of three states, New York, California, and Vermont. New York is a large state with a high ratio of private-to-public enrollment, while California is also a large state, but with a low private-to-public enrollment ratio. Vermont is a small state, with the lowest reliance of public colleges and universities on state government funding.

New York

New York has only lately had a public system of colleges and universities, which explains the high share of enrollment in private institutions. The City University of New York (CUNY) has existed since 1847, but the State University of New York (SUNY) was established only in 1948 (the last such state system). The ratio of enrollment in private colleges and universities to public ones was the fifth highest in the country in 1992-93. However, the ratio slowly declined, from .79 in 1970 to .76 in 1992-93. The historically dominant private sector now finds itself up against increased pressure from the public sector.

New York has 314 institutions of higher education, nearly 10 percent of the nation's total. Its public system is made up of 42 four-year colleges and universities and 47 two-year colleges. Its private sector has 172 four-year colleges and universities and 53 two-year colleges. In 1994-95, total enrollment in the state's four-year private institutions was 393,556, and there were 7,129 students in private two-year colleges. The SUNY system's total enrollment was 195,330 in its four-year system and 196,376 in its two-year system. The CUNY system had total enrollment of 143,866 in its four-year program and 68,768 in its two-year program.

A study of New York's university system found that between 1986-87 and 1992-93 the SUNY and CUNY systems added an additional 44,215 full-time undergraduate students, while the private schools lost 242 similar students.[29] An important reason for the continued trend toward expansion of the public sector at the expense of the private sector is the divergence in tuition between the public and private sectors.

Between 1974 and 1994 the average tuition differential between a private college and the SUNY system increased in current dollars from $1,860 to $10,446. To combat some of the effects of the growing price discrepancy, private colleges and universities have been forced to increase their expenditures on institutionally funded scholarships, thus reducing net tuition revenue. Between 1988 and 1994 gross tuition revenues rose by 52 percent, while net tuition revenues rose only 33 percent. In 1988 college-funded grants were 18 percent of tuition revenues. By 1996 they were 39 percent. In 1995, 97 percent of the increased gross tuition revenue of private institutions went into scholarship aid.[30]

Assistance from New York's Tuition Assistance Program, which provides tuition assistance to students at private colleges, fell from 60 percent of the average student tuition at a private college in 1974 to 31 percent in 1994. Currently, the TAP covers 100 percent of the tuition charged by the state universities. Faced with an increasing tuition gap and limitations in their ability to discount tuition, the independent colleges and universities have been lobbying for an expansion of the TAP program, as well as the state's other two programs that benefit private institutions, the Direct Institutional Aid and Higher Education Opportunity Program grants.[31] Some of the lobbying has been successful. In 1995, $119 million was appropriated for direct aid to the state's private colleges (SUNY received $733.1 million).

Direct public funding of private institutions, although appealing to private institutions when attempting to match revenues to expenditures, comes with a price. A recent headline from the Chronicle of Higher Education is a warning for those institutions wishing to receive state benefits and retain their rapidly eroding independence: "Hearings on Adelphi U. Trigger a Debate about New York's Authority over Private Colleges."

A group of New York state higher education scholars has expressed concern about the trend in New York's higher education system: "The relative cost advantage of New York's public institutions has operated in their favor. They continue to enroll greater percentages of the state's student body each year; the independent sector will most likely educate smaller and smaller percentages of the college population."[32] That is probably an accurate prediction of the future higher education system in the state unless there is a change away from direct state provision of higher education services toward direct aid to students, such as the TAP. It is unlikely that there will be a sudden collapse of the remaining private sector; however, the percentage of students enrolled in the public system will increase. The private schools will rely more and more on federal and state funding to combat the increasing tuition differential, resulting in a reduction in their independence.

California

California has three main systems of public higher education: the University of California, made up of 9 campuses, including the medical school; the California State University system of 22 campuses; and the California Community College system, made up of 106 two-year public institu-

tions. Total enrollment in the 1995-96 school year was 159,202 in the UC system, 330,915 in the California State University system, and 1,378,536 in the California Community College system.[33] Nearly three of four students in public institutions of higher education are enrolled in California's massive community college system.

The private college and university system is less well developed than in New York, although there are 159 private four-year institutions and 39 private two-year colleges. Private institutional enrollment is about equal to the enrollment in the UC system, 186,129 in 1995-96. Thus, the ratio of enrollment in private colleges and universities to public ones, at .10, is much below that of New York.

The private system is maintaining its market share in California. Enrollments in private institutions have risen by 21,301 from 164,828 in 1980-81, an increase of 12.9 percent. Private institutions have lost ground to the UC system, which has increased enrollment by 27,611, or 21 percent. However, the California State University system has increased enrollment by only 13,412, about half the headcount increase of the UC system and a smaller percentage, 4.2 percent. The community college system enrollment has decreased by 4,700, or three-tenths of 1 percent.

As might be expected from a system with a dominant public sector, California has long subsidized tuition at each of its three major systems. In 1965-66 in-state tuition and fees for the UC system were $245 and $105 at the California State University schools, and community colleges were free. By 1971-72 fees at the UC campuses had increased to $640, but they remained relatively stable through that decade. Since 1980-81 UC fees have risen significantly, from $776 to $4,139 in 1995-96, or by more than four times.

A similar pattern exists for the California State University system, with total fees in 1981 of $226, rising to $1,891 in 1995-96, or by almost seven and one-half times. The state university system thus became more expensive relative to the UC system over that time, with the fee ratio going from 29 percent of the UC tuition to 46 percent.

Community college fees have also risen, although they still remain low. The first fees, $100, were charged in 1984-85. Fees were not increased until 1991-92, when they went up to $120. There was an increase to $210 in 1992-93, and $390 in 1993-94, but fees have stabilized at that level.

Private college and university tuition has remained well above that of the state system, although the relative tuition rate decreased somewhat as tuition rose faster in the public system. Weighted average tuition was $1,940 in 1970-71 and $4,610 in 1980-81. Tuition rose to $15,098 in 1995-96, an increase of 2.27 times. The ratio of private tuition to UC tuition has fallen from 5.9 to 3.6. For the California State University system the ratio has gone from 20.3 to 7.98. Private tuition is almost 39 times higher than fees for the community college system.

California has a Cal Grant program, similar to New York's TAP. The program helps needy students with college costs. As has been the case with the New York program, the relative value of the maximum grant has fallen in relation to private college and university tuition and fees. The maximum award went from 69.4 percent of tuition and fees in 1980-81 to 34.8 percent in 1995-96. As is also the case with New York, the percentage of recipients who are in the private system has declined, from 43.7 percent to 28.4 percent. The trends are at least partially a result of the increased reliance of the public system on student fees and the attendant increase in those fees.

From the 1960s to the 1980s the State General Fund accounted for 85-90 percent of total public funding (including student fees) of the California State University and UC systems and, along with local governments, more than 99 percent of the California Community Colleges. In recent years, however, the trend, which is consistent with the national data, has been to rely more on student fees. Over the past 10 years, the proportion of funds made up by State General Fund and local revenues for community colleges has dropped by .8 percentage points, although they still are 93 percent of the funds of the system. Fee revenue has increased by 1.8 percentage points. The California State University system has had a decrease of 9.4 percentage points in its State General Fund share of revenue, while the share covered by fees has increased by 8.7 percentage points. And, at the UC system, the State General Fund share has declined by 16.7 percentage points, while student fee revenue has risen by 12.4 percentage points.

That substantial increase in student fees in the state system has allowed the small private sector to maintain its market share, although the tuition gap remains substantial. That is especially true for the student contemplating a public two-year college. California's system is basically mature, with a private sector approximately equal to the UC system, a state university system about twice the size of

the UC system, and a community college system a little more than four times the size of the state university system. There is more growth in the private sector than in either the state university or community college system, although less than in the UC system. However, given the small total size of the private system, unless there is a major shift toward direct student aid, California's higher education system will continue to be dominated by the public institutions for the foreseeable future.

Vermont

Vermont has had a long history of state institutions since the University of Vermont was founded in 1791. However, it also has one of the oldest private colleges in the country, Middlebury College, established in 1800.

Vermont has 1 public two-year college, 5 public four-year institutions, 2 private two-year colleges, and 14 private four-year colleges and universities. By far the largest public institution is the University of Vermont, with a 1994 total enrollment of 10,230. The next largest of the four-year public schools is Castleton State College, with a 1994 total enrollment of 1,792. The two-year college, the Community College of Vermont, is the second largest public school, with an enrollment of 4,632. Total enrollment in 1994 in the public four-year institutions was 15,590.[34]

The Vermont private system is made up of small institutions. Of the 12 four-year schools, the largest is Saint Michael's College, with a 1994 enrollment of 2,628. Seven of the four-year schools have an enrollment of fewer than 1,000.

Vermont's public colleges and universities have the lowest reliance on state appropriations, with slightly more than 15 percent of current-fund revenue coming from the state government.[35] Public institutions in Vermont rely almost three times as much on tuition and fees as on state appropriations, with 43.5 percent of current-fund revenue coming from student charges. Vermont has the fifth highest ratio of public tuition and fees to private tuition and fees, and by far the highest average undergraduate tuition and fees for public institutions. In 1994-95 the average tuition and fees at public institutions were $5,532, with the next highest state being Pennsylvania at $4,316.[36]

Vermont has one of the highest rates of per capita state aid to undergraduate students in the United States, ranking third in need-based aid at $19.64 compared to a U.S. average of $9.70 and fourth in total grant aid.[37] It provides grants to students through the Vermont Student Assistance Corporation. Vermont has the second highest percentage of state grant aid to students as a percentage of state tax appropriations for higher education operating expenses. Twenty-one percent of the state appropriations for higher education operating expenses go to student grants.

Unlike New York, where the share of tuition assistance funds going to students who enroll in private institutions has been declining, in Vermont the share going to students who enroll in the state's private colleges and universities has remained relatively stable. Vermont allows students to take state financial assistance to out-of-state schools. For fiscal 1996, the share of student grants going to Vermont public students was 32.5 percent; to Vermont private students, 35.7 percent; and to out-of-state students, 31.9 percent. That compares with figures for fiscal 1989 of 35.1 percent, 36.5 percent, and 28.4 percent.

As one would expect in a state where public institutions rely on state appropriations for a low fraction of current-fund revenue, in-state tuition fees and revenues for public institutions are high, and a higher education program has a larger-than-average component of direct student aid, Vermont has one of the nation's strongest private educational systems. Its ratio of private to public enrollment is the sixth highest at .73, for 1992-93, with only Massachusetts being significantly higher, at 1.32. The ratio has been fairly stable over the last quarter century. In 1970 the ratio of private to public enrollment was slightly higher, .77. However, for the period 1989-90 to 1992-93, the growth in enrollment in private institutions exceeded that of public institutions, both in percentage terms, 2.6 percent to .4 percent, and absolute enrollment, 383 to 76.

The Vermont experience shows that the state's policy of funding its public higher education system through tuition and fee revenues, and making student aid a larger share of state spending on higher education, can result in a system of higher education that is much more balanced toward the private sector.

The Importance of Private Higher Education

Why is it of any consequence that we have moved from a system of higher education that was primarily private (there were only 21 fully established state government colleges and universities before the Civil War) to one in which the vast majority of students attend government-operated institutions of higher education?[38] There are several reasons, some of which have to do with economic efficiency; others have to do with the independence of our higher education system.

Special Characteristics of Private Colleges

John Ashcroft and Clark Kerr made a strong case for the importance of private higher education in their 1990 report, The Preservation of Excellence in American Education: The Essential Role of Private Colleges and Universities.[39] They point out that private institutions offer a diversity of mission that is not and, in some cases, cannot be offered in the public sector. Ninety-five percent of the nation's liberal arts colleges are private. Almost 800 private colleges and universities have a religious affiliation, and many more have a curriculum grounded in religious values. About 200 private colleges offer single-sex education. While public institutions tend to be large, private colleges offer a small-school educational experience. Eighty-five percent of colleges that enroll fewer than 1,000 students are private. Private colleges are an important part of the nation's graduate school program, awarding nearly half of all Ph.D. degrees.

Private schools, smaller and less encumbered by bureaucracy, are able to respond to changes in market demand more swiftly than public institutions. The private sector, since it cannot rely on tax revenue to survive, is driven to innovate. Kerr and Ashcroft conclude, "Overall, private institutions encourage the continuance and further development of a total system that is more competitive, more diverse, more dynamic, more cost-effective and of higher quality than it would otherwise be."[40]

Breneman has made the case for private liberal arts colleges. He cites research showing that students at those institutions are more likely to interact with faculty and get involved in college life. Students at private colleges are more satisfied with classroom instruction and faculty-student contacts. Small liberal arts colleges place students in Ph.D. programs at a highly productive rate. Students at private colleges and universities complete their

degrees at a much higher rate than their counterparts at state-run institutions. And independent colleges serve all ranges of the income distribution. In fact, the median family income of students in state and independent four-year institutions is identical.[41]

Maintenance of the Social Order

Aside from specifying the positive attributes of private colleges and what would be lost if they were to disappear, one can make the case that an independent private college system is necessary to maintain our free society and our constitutional republic. There are a variety of answers to the question, "What is the purpose of higher education?" and pluralism is probably the main reason that we must maintain a private college alternative to state-run institutions. For the role of state institutions is, and must be, to follow the mandates of the political system. But the temptation of a government system is to produce like-minded individuals, often succumbing to a trade-school mentality. In remarking on the need for an education emphasizing ethics and a moral principle, Benjamin Disraeli said in 1839:

> By their system of state education all would be thrown into the same mint, and all would come out with the same impress and superscription. They might make money, they might make railroads; but when the age of passion came, when those interests were in motion, and those feelings stirring, which would shake society to its centre, then . . . they would see whether the people had received the same sort of education which had been advocated and supported by William of Wykeham.[42]

Agreeing with Disraeli, John Henry Newman wrote, "The problem of statesmen of this age is how to educate the masses, and literature and science cannot give the solution."[43] Given that it still appears that educating the masses is the problem of statesmen, it is essential that colleges and universities exist that can do more than educate in science and letters. State-run institutions are not likely to take up this challenge. Taxpayers are more likely to support "literature and science" and training people for a trade.

That leaves a burden on the private, independent colleges and universities to carry on and discuss the ideal and vision of tradition and morality, as well as the innovative minority viewpoint of the independent thinker. It is diffi-

cult to believe that such an education could be the focus of a state-run institution, regulated by the legislature and relying on the political system for its maintenance and support. It is private colleges that hold the key to maintaining a civil society when "the age of passion" has arrived.

Private, independent institutions of higher learning are a part of, and preserve the foundations of, a civil society. A civil society is one in which people rely on the natural and voluntary associations that form the social order. Alexis de Tocqueville described the United States of the mid-19th century as a society in which Americans constantly joined with one another to solve their everyday problems and to provide services and camaraderie. The private college has been one of those associations from the beginning of the colonies. It is not within government-owned universities, but rather within the private colleges, that solutions to social problems that rely on voluntary cooperation, and thus civil behavior, are likely to emerge.

Economic Efficiency

It is also true for economic reasons that higher education services are best provided by the private sector rather than by state governments. James Buchanan and Nicos Devletoglou analyzed the economic inefficiency of direct provision of higher education by state governments in the context of their discussion of the student rebellion of the 1960s.[44] Their point is that we have created a system in which the vast majority of students attend college for a price that is far below the true cost of providing that service, the service is not sold by those producing it, and the service is not controlled well by those who own the institution at which it is provided.

There are several problems with providing a service below cost, many of which are analyzed in any elementary economics text. The primary point is that the value to the consumer is less than the value of the resources being used in providing the service. That is economically inefficient, since those resources could have been used to produce something that consumers prefer. At public colleges and universities, clearly students are not charged the true cost of providing the service. Buchanan and Devletoglou make the point that because students are not charged the true cost of their education, they will have less incentive to make good use of the services of the college and "the result is that a sizable proportion of university students, under any low

tuition scheme, will be placing less value on what they are enjoying than they would place on other uses of these resources."[45]

In the case of state-owned universities, if not all students are admitted that wish to enter at the tuition being charged, the space available will be rationed on the basis of some set of admission criteria. If the price mechanism is not used as a rationing device, other methods will be. Those criteria can be set any number of ways, depending on how closely the legislative branch oversees the university system. Slots could be allocated on the basis of estimates of academic performance, such as high school grades, letters of recommendation, and entrance exams. However, as Dinesh D'Souza has detailed in Illiberal Education, other criteria, such as race and socioeconomic status, also can be used.[46] Since the political system is, in the final analysis, the method of allocating slots, it should come as no surprise, for example, that the UC used to set aside certain slots for some minority groups and limit the slots for other minority groups.[47] In any case, the rationing mechanism will be less efficient than if consumers simply bid for the open slots in a private market.

Another less obvious result of rationing by other than price is analyzed by Mitchell and Simmons in their explanation of Charles Sykes's description of some of the failings of state-run universities.[48] Mitchell and Simmons make the point that state universities do not participate in the free market in the way that private schools do; rather, state universities participate in a process funded by taxpayers and controlled by state officials. The setting of tuition below the market-clearing level allows the professors to collect a "rent" in the form of inflicting nontuition costs on students. Those include having to endure larger class sizes and having teaching assistants teach the classes so that professors can do research.

Private colleges may not set tuition levels at market-clearing prices either. It is not easy to know how much of the excess demand for slots at elite high-priced private colleges is truly excess demand. While the "retail price" of tuition may be high, prospective students applying for admission often assume that they will receive a discount in the form of scholarship aid. It could be that much of the excess demand comes from students believing that tuition will be less than the actual price.

Nonetheless, private colleges charge much closer to the cost of providing the service. Tuition and fees, along with

the sales of services such as residential facilities and hospitals, provide nearly two-thirds of the revenue of private colleges and universities, compared with slightly more than two of five dollars of current-fund revenue for the public sector.[49] And private institutions discount their tuition to a greater extent, with scholarships and fellowships making up about three times as large a percentage of current-fund expenditures as they do for public institutions.[50]

Buchanan and Devletoglou make the point that those producing the service of public higher education do not sell the product. Neither the professors nor the board of regents or trustees that controls public colleges and universities are in the business of selling teaching services to students. Public institutions of higher education do not generally market themselves, and tuition policy depends on state appropriations rather than profit maximization. Much has been written about the fact that professors are not rewarded on the basis of their teaching services.[51] Many of the characteristics of today's higher education system detailed in the recent exposés can be traced to that factor. In fact, one might find the following statement in any of the recent books on the academy:

> If the teacher happens to be a man of sense, it must be an unpleasant thing to him to be conscious, while he is lecturing his students, that he is either speaking or reading nonsense, or what is very little better than nonsense. It must too be unpleasant to him to observe that the greater part of his students desert his lectures; or perhaps attend upon them with plain enough marks of neglect, contempt and derision.[52]

Yet that was written by Adam Smith over 200 years ago. Smith's commonsense solution was to have at least a portion of the faculty member's salary dependent on tuition from his students. The discipline of the market ensures at least some attention to the demands of the consumer. The point is that moving to a market-based allocation of higher education resources, rather than a publicly provided one, will result in a better match of consumer demand and producer supply.

The third point made by Buchanan and Devletoglou is that the owners of the state higher education system do not control the product and cannot effectively decide on resource allocation. William Niskanen provides the definitive discussion of the problem of incentives of bureaucrats in providing services and the asymmetry of information in the

case of government-supplied goods.[53] Bureaucrats, for various reasons, have an incentive to maximize the size of their budgets. That is surely the case in higher education where prestige, salaries, and academic rents are often greater in institutions with higher budgets than in those with small budgets.

According to Niskanen's theory, the legislature, which sets the appropriations for the bureau, has little knowledge about the true minimum cost of providing the services, or at least has less knowledge than the bureaucrats who run the institutions. Again, that is surely the case for higher education services. The legislature has much less knowledge of what it takes to educate a student than does the state university. Niskanen has shown that under such circumstances, there will be an expansion of the bureau's budget beyond that necessary to satisfy the preferences of the legislature. The result, in this particular case, is that state university systems will have higher budgets than would be preferred by the legislature and at a higher cost of output than is efficient.

Martin Anderson, author of Impostors in the Temple, is among those who have argued that private colleges and universities, since they are nonprofit, act much like public colleges and universities.[54] Meiners and Staaf provide an economic analysis relying on a model of property rights markets in higher education to show that private nonprofit colleges will not behave in the same way that private for-profit colleges would.[55] Their conclusion is that private colleges may be more efficient than public colleges, but they will have many of the characteristics that public universities have.

Although private nonprofit institutions of higher education may be less efficient than for-profit colleges would be, they are likely to be much more efficient than state-owned institutions. Second, since nonprofit colleges and universities cannot be modeled as profit-maximizing firms, as Ludwig von Mises pointed out in his work on bureaucracy, the difference between the private sector and the public-sector bureaucracy is large.[56] The reason is that, in the end, the private sector is forced to face up to market signals in the form of profits and losses. Although the incentives for administrators and faculty may be similar in the public and private sectors, the constraints on the private sector are much stronger. Even though private colleges may be nonprofit, they can still go out of business. In fact, of those private colleges that had opened

their doors before the Civil War, in many states 80 percent or more had closed by 1928.[57]

Direct government provision of higher education is not only economically inefficient within its own sphere; it also alters the behavior of private-sector colleges and universities, making them less efficient. Private colleges and universities seeing salary costs rising in part because of the demand for faculty in the public sector, and facing a marked disadvantage in tuition, will be forced to seek sources of revenue other than charging their students.

Aside from tuition, the three main sources of revenue are the federal government, state governments, and foundations. Private colleges thus are forced to lobby for money from governments, both state and federal, and to seek foundation grants.

Several works have identified the growth in federal support for higher education and its effect on private colleges. Roche examines the increased reliance on government funding.[58] He points out that federal aid, up until the 1960s, consisted primarily of research grants and contracts to colleges. Then the 1960s saw a major expansion in student assistance as part of a 400 percent increase in federal higher education spending. Over the last 25 years the number of students receiving federal grants has doubled and the number of federal loans tripled. The federal government today provides nearly 75 percent of student financial aid. Roche argues that this reliance on federal aid threatens the independence of the higher education system.

Meiners has speculated that private colleges and universities have a greater incentive to lobby for federal dollars than do public institutions.[59] Private colleges and universities do rely to a greater extent on the federal government for current-fund revenue than do their public competitors, 14.9 percent in 1992-93 compared to 10.8 percent. That does not include Pell grants and other federally supported student aid. The public and private sectors are about equally reliant on that aid. Federal student aid makes up about 2 to 3 percent of current-fund revenue for both sectors.

Private colleges and universities, while, as noted above, relying on state government for only a small portion of their total revenue, saw that reliance increase from $430 million in 1980-81 to nearly $1.5 billion in 1992-93. The lion's share of the growth was in restricted grants and contracts.

It is easy to find examples of lobbying efforts by associations of private colleges and universities to increase state aid. As an example, the Coalition for Independent Colleges and Universities in the state of New York has vigorously pursued expansion of state support for private colleges.

The third place that private colleges have turned for revenue is foundations. The growth of giant foundations began in the early 1900s. Two of the early large contributors to higher education were Rockefeller's General Education Board, which began in 1905 with $10 million, and the Carnegie Foundation, founded in 1906 with $31 million. Foundation money has always tended to be concentrated at a relatively small number of larger or more prestigious schools. As noted by George Stigler, the problems with relying on foundation money include a biased distribution of research scholars toward the foundation-supported schools and negative effects on the type of research and curriculum provided at colleges and universities.[60]

A major problem with the resort of private colleges to nontuition support is the loss of independence of the private college. By being forced to seek out sources of revenue other than tuition to compete in price with the public colleges, private colleges move away from the Adam Smith notion of fee for service and into arenas where they will become dependent on the wishes of large foundations or the whims of the federal and state governments.

Ronald Kimberling warns, "On a larger scale, academic administrators must begin to ponder the issue of how dependence on federal student aid monies has opened the door for significant federal regulation of academic and administrative matters hitherto the province of individual institutions."[61] Buchanan and Devletoglou opine, "Without massive and continuing financial support from the community at large, the modern university as presently constituted would swiftly collapse."[62] They point out that Kerr called private universities federal grant universities, because of their dependence on federal dollars.

Solutions

There are a number of ways to deal with the effects of public universities on the higher education system in the United States. First, we might take the view that it is not the proper role of government to be involved in the production of higher education, since government will have gone

beyond its just role of the protection of life, liberty, and property.[63]

We might also take the view that the externality argument, that higher education provides a benefit for society in excess of that captured by the student and thus should be subsidized, is not valid. For example, West makes this case in regard to K-12 education. Others argue that even if the externality argument were true for K-12, it is not true for higher education where enough of the benefit is internalized to the student consumer that he or she will purchase an efficient amount without government subsidy.

The logical policy prescription for these views is that we sell off the public colleges and universities to the private sector and allow the market to determine the amount of higher education that will be produced and consumed. However, this solution is clearly not politically feasible.

In the current political climate, it is reasonable to ask, assuming that higher education will be provided by state governments, how this service should be provided. Note that state provision for services does not require state production of services. It may well be that we can think of privatizing the higher education function (or more precisely, reprivatizing it) in the same way that we can think of a city's accounting services.

That would necessarily take place over time, since public universities now make up 80 percent of the market and it would be surprising if private entrepreneurs could in the short run make use of that capacity.[64] The state either would purchase the service of higher education directly from private colleges or would provide G.I. bill-like tuition vouchers for its students to use at private colleges. Again, this scenario is unlikely, whether it makes sense or not.

The most practical policy option that would solve some of the problems with today's higher education and reduce the misallocations caused by the unintended effects on private colleges is to eliminate the direct subsidies to public universities, require the universities to charge tuition sufficient to cover costs, and give financial aid to the students. That would place private and public colleges on an even footing, since the tuition at both types of institutions would be equally subsidized. Taxpayers would no longer be subsidizing wealthier families and moving them away from private schools. It would also require state-run colleges and universities to face the prospect of closing

down if their expenses were not covered by tuition and other revenue sources. Thus, the market would serve its important function of taking resources away from those entrepreneurs that do not make valuable enough use of them.

Before analyzing the effects of this proposal in more detail, it must be noted that this is not by any means a new idea. The Newcastle Commission on Popular Education was set up in 1858 in Great Britain to examine the efficacy of the education system of Great Britain, which at that time was entirely private. The commission came to the conclusion that the best policy was not to set up government schools but rather to provide direct subsidies to the existing private schools. Although that is not the same proposal that has been laid out in this analysis, it is consistent with the position that education is better provided through government subsidy of education than creation of government institutions to provide education directly.

More than 20 years ago, Stephen Tonsor of the University of Michigan, in a paper prepared for a conference on higher education, argued, "Until the United States has a system of full-cost tuition paid by every student, we will not have rationality and order in the university world."[65] He then suggests a program of loans to students for tuition and other educational costs, to be repaid with a tax on future income.

Buchanan and Devletoglou argue in support of an alternative system of student loans, rather than direct subsidies to a government higher education system that then provides services at zero or below-cost prices. Their point is that students would be forced to recognize the scarcity value of the resources going into higher education and they would change their behavior for the better. They remark upon the attempt of the Russian government to give away bread. The result was that the peasants began feeding the bread to their cattle. The case will be the same for university education: if it is provided free or substantially below cost, it will be used to excess.

One particular method of providing for student loans has been put forth by John Silber, former president of Boston University. The government would advance any undergraduate up to 75 percent of tuition costs for up to four years. Repayment would come to the Internal Revenue Service from withheld taxes. To reduce the effect of such a program on tuition, the maximum increase in tuition that would be financed under the program would be tied to the Consumer Price Index.

Requiring state colleges and universities to sell their services to the public would reduce the problems discussed earlier, as students would now choose among universities on the basis of the education they received relative to the cost of producing that education. Universities would allocate their resources to attract students, reducing costs and innovating to provide a product superior to that of their competitors. Buchanan and Devletoglou note the lack of innovation when private colleges are forced to compete with state-financed universities. Those that want to start a new college are faced with nearly insurmountable barriers in attempting to recruit faculty from the state-subsidized schools, and they would have difficulty establishing the superiority of their product over that which could be obtained for much lower out-of-pocket cost. As Buchanan and Devletoglou put it, "The degree of differentiation in product would have to seem immense to the prospective purchaser to induce much switch of custom."[66]

One of the primary reasons that markets are efficient is that people who make poor or inefficient uses of resources go out of business and no longer control those resources. Others who make better use of resources continue to produce. State-owned universities and colleges do not go out of business because of poor use of resources. In an extreme case, a state institution will be closed down, but as all government decisions are political, the closing of a government campus is a political decision, not an economic one. On the other hand, private colleges do go out of business if they are not able to generate enough revenue from their customers or from their donors to meet the cost of the resources they use up. There is a limit to the inefficiency of private higher education.

Aside from increasing efficiency, moving to a full-cost tuition program matched with student loans would reduce the amount of income redistribution that occurs from the less wealthy to the wealthy through a state-owned university system. It has long been known that government support of higher education tends to redistribute income from the poorer classes to the wealthier classes. In 1845 a Virginia newspaper complained about state appropriations for the university at Charlottesville, arguing that the funds could be better used for other things than for providing instruction to "youths, all of whom have the means of finishing their course through their own resources."[67] Any casual observer of a public university campus will see that those who attend college tend to be in the upper half of the socioeconomic distribution. For example, 52 percent of SUNY students had gross family income of more than $50,000.

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Moving to a system of student loans would at least reduce the magnitude of that type of redistribution.

If the political will is to use the higher education system as a scheme for the redistribution of wealth from the higher incomes to the lower incomes, then, rather than provide free or below-cost tuition for all through a state-owned system, state aid could be given directly to students on the basis of income. This would allow the state universities to capture some of the consumer surplus of students, thus reducing the cost to taxpayers of a given level of state higher education. Those students willing to pay or capable of paying full-cost tuition are currently receiving consumer surplus that could be reduced through full-cost tuition charges. Need-based aid could be accomplished through a government loan system with the loan payback dependent on the wealth of the student's family. The important feature of an aid-based system would be that aid go directly to the student rather than to the university.

There are real political costs involved in switching from a system of direct funding of institutions to aid for students. These will occur, for one reason, because of transition costs. Thousands of public colleges and universities have been set up under the existing system. They will have to change their behavior and will have entirely different incentives under a full-cost tuition with loans or scholarship programs. The details of the program would have to include what to do about current capital costs. Would the state continue to provide for the amortization and maintenance of existing facilities? Under a competitive scheme, many institutions would be a different scale than they are now. These institutions will be burdened with an overbuilt infrastructure that cannot be financed under a tuition scheme.

There will also be the political cost of having public universities close down. Throughout our history, the presence of a university has provided certain benefits and prestige to a town. The fact that so few state colleges and universities have closed their doors in the past 20 years is an indication that state and local politics weighs heavily in such a decision. Suppose the University of Michigan were faced with a financial crisis under a switch to tuition-based financing. Would the Michigan legislature provide bailout? The answer, probably, is yes. However, less prestigious schools, such as Lake Superior State University, might be allowed to close or be turned over to the private sector.

Nonetheless, transition problems are not insurmountable. The Michigan legislature could provide larger scholarships to those who attend the University of Michigan over the transition period, for example. At least the system would be moving in the right direction and the belief that institutions of higher education should seek to attract consumers through efficient provision of services would begin to filter through to the general populace. This in itself would lead to a more enlightened discussion of the role of government in education and what the optimum structure should look like.

Conclusion

The problems of private higher education have been to a certain extent a result of the existence and expansion of the public university system and the private college response. It is becoming increasingly documented that higher education is foundering. Only one in five business respondents to a survey by Professor Patrick Scheetz rated new college graduates as "adequately prepared" for the current job market.[68] Barton and LaPointe, in Learning by Degrees: Indicators of Performance in Higher Education, find that nearly half of college graduates function at less than an eighth-grade reading level.[69]

A large improvement can be made in the situation by returning to the marketplace for the provision of higher education. Private independent colleges and universities provide the anchor for this return. By moving to a system of consumer choice through full-cost tuition and scholarships, there will be a renewed responsibility to satisfy the consumer-student rather than to choose a strategy of defensive rent seeking.

State-owned and state-operated colleges and universities have altered the structure of private education and threaten its long-term independence. A free society requires an arena in which the study of ideas and their transmission to the populace can occur free from government intervention. The words of Daniel Webster in arguing the case for Dartmouth before the U.S. Supreme Court make the case for private colleges today as well as they did more than 175 years ago:

> It is the case, not merely of that humble institution, it is the case of every college in the land. It is more. . . . Sir, you may destroy this little institution, . . . but if you do . . . you must

> extinguish, one after another, all those great lights of science, which, for more than a century, have thrown their radiance over the land![70]

The current debate about higher education has created an opportunity to focus on the importance of our private system of colleges and universities and recognize that the massive subsidies to government-owned institutions have threatened the existence of a truly independent arena for the education of the next generation of our nation's leaders.

Notes

1. George Roche, The Fall of the Ivory Tower (Washington: Regnery, 1994), p. 259.

2. John Stuart Mill, On Liberty (1859; New York: Norton Critical Edition, 1975), p. 98.

3. It is easy to see the practical problem in squaring Russell Kirk's contention that "a principal achievement of liberal education in America has been the imparting of a sense of moral worth among those who lead intellectually" with the curriculum that can be offered at an institution run and maintained by state government. See Russell Kirk, "The Revitalized College: A Model," in Education in a Free Society, ed. Anne Burleigh (Indianapolis: Liberty Fund, 1973).

4. See Frederick Rudolph, The American College and University: A History (New York: Alfred Knopf, 1962), pp. 254-55, for a discussion of how this position was inconsistent with the fact that both those institutions were heavily subsidized by government in their early years.

5. William Zumeta, "State Policies and Private Higher Education," Journal of Higher Education 63, no. 4 (July-August 1992): 363-417.

6. Dollar amounts in this discussion are from U.S. Department of Education, National Center for Education Statistics, Digest of Education Statistics, various years.

7. There are other ways to measure the tuition gap, for example, the ratio of public to private tuition, or more complicated measures, such as the income-deflated gap used by Michael McPherson, "The Demand for Higher Education," in

Public Policy and Private Higher Education, ed. David Breneman and Chester Finn (Washington: Brookings Institution, 1978). However, any measure will demonstrate substantial differences in tuition and fees for public and private institutions.

8. General Accounting Office, Higher Education, "Tuition Increasing Faster Than Household Income and Public College's Costs," GAO/HEHS-96-154, pp. 43-45.

9. Ibid., pp. 40-43.

10. Ibid., pp. 66-68.

11. McPherson, p. 183.

12. Ibid., pp. 190-91.

13. Charles Manski and David Wise, College Choice in America (Cambridge, Mass.: Harvard University Press, 1983).

14. Larry Leslie and Paul Brinkman, "Student Price Response in Higher Education," Journal of Higher Education 58, no. 2 (March 1987): 181-204.

15. Michael McPherson and Morton Shapiro, Keeping College Affordable (Washington: Brookings Institution, 1991), p. 103.

16. Ibid., pp. 103-4.

17. Philip Ganderton, "The Effect of Subsidies in Kind on the Choice of a College," Journal of Public Economics 48 (1992): 269-92.

18. Charles Kroncke Jr. and Rand Ressler, "The Alchian-Allen Effect in Higher Education: Public versus Private Enrollment," Economics of Education Review 12, no. 4 (1993): 345-49.

19. Christopher Lucas, Crisis in the Academy: Rethinking Higher Education in America (New York: St. Martin's, 1996), p. 14.

20. Editors of U.S. News and World Report, America's Best Colleges: The 1997 Directory of Colleges and Universities.

21. Several forms of the regression model were estimated, using standard variables, such as those found in John Quigley and Daniel Rubinfeld, "Public Choices in Higher Educa-

tion," in Studies of Supply and Demand in Higher Education, ed. Charles Clotfelter (Chicago: University of Chicago Press, 1993), pp. 243-83. The regression finally estimated was PRIPUB = -.11 + .0002 PT - .05 PUR + .03 PRR, R^2 = .60, where PRIPUB is the ratio of private to public college and university enrollment, PT is in-state tuition at four-year public colleges and universities, PUR is the number of public institutions ranked by USNWR, and PRR is the number of private colleges and universities ranked by USNWR. The data are for the 1993 academic year, other than the rankings, which are for 1997. The standard errors of the coefficients are .00003 for PT, .022 for PUR, and .008 for PRR.

22. Data include branch campuses. Source is U.S. Department of Education, National Center for Education Statistics, Digest of Education Statistics, 1995.

23. Carnegie Foundation for the Advancement of Teaching, A Classification of Institutions of Higher Education (Princeton, N.J.: CFAT, 1987).

24. Unpublished data.

25. David Breneman, Liberal Arts Colleges: Thriving, Surviving, or Endangered? (Washington: Brookings Institution, 1994), pp. 11-13.

26. E. G. West, Education and the State: A Study in Political Economy, 3d ed. (1965; Indianapolis: Liberty Fund 1994), chap. 10.

27. Quoted in ibid., p. 174.

28. Ibid., p. 193.

29. Coalition for Independent Colleges and Universities, The Commitment and Capacity to Serve New York State (Albany: CICU, December 1994).

30. Ibid.; and Coalition for Independent Colleges and Universities, There's a Cost-Effective Solution to New York's Fiscal Problem (Albany: CICU, November 1995).

31. Ibid.

32. William C. Barba et al., "Factors That Shaped Higher Education in New York State: A Historical and Current Perspective," in Higher Education in Crisis: New York in National Perspective, ed. William C. Barba (New York: Garland, 1995), p. 11.

33. Data for this section are primarily from California Postsecondary Education Commission, "Fiscal Profiles, 1996," Commission Report 96-7, September 1996.

34. Data on 1994 enrollment are from New England Board of Education, "Facts 1996," Connection 10, no. 3.

35. Data for the rest of this section are from Digest of Education Statistics, various issues, and author's calculations.

36. It might be noted that Pennsylvania has a slightly higher ratio of private to public enrollments than does Vermont, at .766.

37. New England Board of Education, Table 93. All of Vermont's student aid is need based.

38. For the history of American higher education, see Rudolph; see also Donald Tewksbury, The Founding of American Colleges and Universities before the Civil War (New York: Arno, 1969).

39. John Ashcroft and Clark Kerr, chairmen, The Preservation of Excellence in American Higher Education: Report of the ECS Task Force on State Policy and Independent Higher Education (Denver: Education Commission of the States, 1990).

40. Ibid., p. 11.

41. Breneman, pp. 3-11.

42. Quoted in Russell Kirk, The Conservative Mind from Burke to Eliot, 7th rev. ed. (Washington: Regnery, 1986), p. 293.

43. John Henry Newman, "The Tamworth Reading Room," quoted in ibid., p. 279. See also John Henry Newman, The Idea of a University, ed. Frank M. Turner (1899; New Haven, Conn.: Yale University Press, 1996).

44. James Buchanan and Nicos Devletoglou, Academia in Anarchy: An Economic Diagnosis (New York: Basic Books, 1970).

45. Ibid., p. 29.

46. Dinesh D'Souza, Illiberal Education: The Politics of Race and Sex on Campus (New York: Free Press, 1991).

47. That practice has apparently been halted as of the 1997-98 school year by action of the University of California Board of Regents.

48. William Mitchell and Randy Simmons, Beyond Politics (Boulder, Colo.: Westview, 1994), pp. 118-26, and the references contained there.

49. Digest of Education Statistics, 1995, Tables 319 and 320.

50. Ibid., Tables 330 and 331.

51. Charles Sykes, Profscam (Washington: Regnery, 1988), and Charles Sykes, Hollow Men (Washington: Regnery, 1990), are but two of the books on the subject.

52. Cited in Roger Meiners, "The Evolution of American Higher Education," in The Academy in Crisis, ed. John Sommer (New Brunswick, N.J.: Transaction, 1995), p. 21.

53. William A. Niskanen Jr., Bureaucracy and Representative Government (Chicago: Aldine-Atherton, 1971).

54. Martin Anderson, Impostors in the Temple (New York: Simon and Schuster, 1992).

55. Roger Meiners and Robert Staaf, "Property Rights in Academe," in The Academy in Crisis.

56. Ludwig von Mises, Bureaucracy (1944; Cedar Falls, Iowa: Center for Futures Education, 1983), pp. 31-36.

57. Tewksbury, pp. 27-28.

58. Roche.

59. Meiners, p. 40.

60. Cited in ibid., pp. 38-39.

61. Ronald Kimberling, "Federal Student Aid: A History and Critical Analysis," in The Academy in Crisis, p. 92.

62. Buchanan and Devletoglou, p. 62.

63. For proponents of such a position, see Benjamin Rogge and Pierre Goodrich, "Education in a Free Society," in Education in a Free Society.

64. Of course, one might argue that we have a good deal of overcapacity since the tuition at public universities is set artificially low. Thus, the private sector may never make use of the entire stock of public university seats.

65. Stephen Tonsor, "Rationalizing the Financing of Higher Education," in The Idea of a Modern University, ed. Sidney Hook, Paul Kurtz, and Miro Todorovich (Buffalo: Prometheus Books, 1974).

66. Buchanan and Devletoglou, p. 174.

67. Quoted in Rudolph, p. 213.

68. Patrick Scheetz, "Recruiting Trends 1994-95: A Study of Businesses, Industries, and Governmental Agencies Employing New College Graduates," Michigan State University, Collegiate Employment Research Institute, 1995.

69. Cited in Thomas Bertonneau, Declining Standards at Michigan Public Universities (Midland, Mich.: Mackinac Center for Public Policy 1996), p. 8.

70. Quoted in Rudolph, pp. 209-10.

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